ORIGINAL

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Implementation of Section 402(b)(2)(A) of the Telecommunications Act of 1996	)	**CC Docket No. 97-11**
	)	
	)	

REPLY COMMENTS

Lawrence Fenster
MCI Telecommunications Corp.
1801 Pennsylvania Ave., NW
Washington, DC 20006

March 17, 1997

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Summary

The Commission has historically interpreted Congressional intent with regard to its Section 214 procedures as including a concern that investments might be used in a discriminatory fashion. Moreover, Congress viewed Section 214 processes as a complement to the Commission's cost allocation, separations, and separate subsidiary requirements, rather than being superseded by these other regulatory tools.

In this proceeding, incumbent LECs (ILEC) focus exclusively on whether Section 214 procedures are needed to protect against duplicative investment. They conclude that since the incentive for duplicative investment is limited to companies regulated under rate of return regulation, Section 214 procedures are no longer needed to protect captive ratepayers of price cap LECs. Incumbent LECs have failed to consider the anticompetitive effects of discriminatory investment and discontinuance of service in their evaluation of the Commission's Section 214 procedures. The incentives for discriminatory investment will certainly increase in the current era. Incumbent LEC proposals would leave the Commission without *ex ante* tools to prevent such abuses.

Whatever action the Commission takes with regard to its Section 214 procedures should preserve *ex ante* review of ILEC investments and discontinuances. MCI believes the Commission will strike the right balance between promoting competition, protecting consumers, and reducing regulatory burdens by retaining its Section 214 review for price cap and average schedule LECs while granting them increased filing flexibility, and streamlined reporting requirements.

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REPLY COMMENTS

I. Introduction

MCI Telecommunications Corporation ("MCI") respectfully submits its reply comments in response to the Notice of Proposed Rulemaking ("Notice") in the above-captioned docket[1]. In response to its Notice, the Commission received comments from 16 parties representing the major interests affected by this Section of the Telecommunications Act of 1996 (1996 Act). These parties include: price cap incumbent local exchange companies (LECs); average schedule incumbent LECs; potential Incumbent LEC competitors; and one state regulator. After assessing initial comments, MCI has identified 3 issues to which it wishes to reply: (1) the failure of incumbent LECs to address discriminatory investment and discriminatory discontinuance of service; (2) the failure of incumbent LECs to properly apply legislative criteria for forbearance; and (3) the distinction between a line extension and

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[1] *In the Matter of Implementation of Infrastructure Sharing Provisions in the Telecommunications Act of 1996*, CC Docket 96-237, FCC No. 96-456, released November 22, 1996.

a new line.

II. Incumbent LECS Would Eliminate the Tools Needed to Prevent Discriminatory Investment

As MCI explained in its comments, a firm regulated under rate of return regulation has an incentive to engage in wasteful, duplicative, investment in order to inflate its rate base and increase rate levels; while a firm attempting to forestall competitive entry into its core markets has an interest in making inefficient investments in excess capacity in order to support targeted, anticompetitive, price reductions. Incumbent firms may also make discriminatory investments that are designed to thwart the efficient operations of their competitors, or favor their affiliates, independent of whether the investments are inefficient for their own networks. Under existing conditions of potential competitive entry into the local services market, the incentives for incumbent LECS to engage in these types of anticompetitive investments are greatly increased. Only *ex ante,* Section 214, investment review can protect against these anticompetitive behaviors.

Incumbent LECS fail to consider the possibility that discriminatory investment and investment in excess capacity could be used to foreclose competitive entry. The presence of this behavior is eloquently attested to in the Comments of Digital Network Services, Inc. (DNSI) DNSI describes Southwestern Bell's (SWB) plans to eliminate aspects of its Operator Transfer Service that are essential for DNSI's provision of long distance service in SWB's service territory,[2] thereby discriminating in favor of SWB's

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[2] *See*, DNSI Comments at 5.

eventual entry into the in-region long distance market.

Just as disinvesments and discontinuances may serve a discriminatory, anticompetitive purpose, so may investments. Parties proposing that the Commission forbear from its Section 214 authority limit their discussion to the likelihood of duplicative, gold-plated investments occurring in the absence of Section 214 procedures.[3] To date, no party has contested MCI or DNSI's evidence that discriminatory and anticompetitive investments occur, and that only Section 214 procedures can protect in advance against the damage these behaviors would otherwise cause.

III. Incumbent LECS Do Not Properly Apply Legislative Criteria that would Justify Forbearance

In its Notice, the Commission identifies the conditions it must meet in order to exercise its forbearance authority.

> "Section 10(a) directs the Commission to forbear from enforcing a regulation or provision of the Communications Act when: (1) enforcement is not necessary to ensure that the charges, **practices**, classifications, or regulations by, for, or in connection with a carrier or service are just and reasonable and not unjustly or unreasonably discriminatory, (2) enforcement is not necessary to protect consumers...Section 10(b) further instructs the Commission to consider whether forbearance will promote competitive market conditions and **enhance competition** among providers of telecommunications services."[4] (emphases added)

Incumbent LECS recognize that it would not be appropriate to forbear from procedures

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[3] *See*, Comments of: USTA at 3; GTE at 7; SWB at 3; BellSouth at 7; Ameritech at 5; Pacific Telesis at 7; US West at 5; Bell Atlantic and NYNEX at 3.

[4] *Notice* at para. 39.

that protect against discriminatory investment, but they contend that Section 214 procedures are not designed to protect against this sort of discrimination.[5] Incumbent LECs are simply incorrect on this point. As MCI showed in its initial comments, the Commission has used Section 214 to prevent discriminatory investments.[6] Moreover, discriminatory practices affecting the provision of service remain an ongoing concern, as DNSI's comments confirm. Since investment can be discriminatory, and since only Section 214 review can be used to protect in advance against discriminatory investment, there is no justification for the Commission to forbear from exercising its Section 214 authority.

Incumbent LECS also recognize that it would be inappropriate to forbear from procedures that are needed to protect consumers, but argue that Section 214 is not needed to protect consumers of price cap LECS from unreasonable rates, since price caps allegedly sever the relation between investment and rates.[7] Incumbent LECs are wrong when they assert that price caps sever the relation between investment and rates. If price cap LECS intend to overinvest in order to foreclose competitive entry, they would choose the sharing option and would be partly compensated for overinvestment if the low-end adjustment is triggered. The possibility this will occur will

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5 *See*, Ameritech Comments at 14: "... the Section 214 process is not needed to ensure that a price cap carrier's charges, practices and classifications remain just and non-discriminatory." See also, Bell Atlantic/NYNEX Joint Comments at 3; and Pacific Telesis at 9.

6 *See*, MCI Comments at 4.

7 *See*, Comments of: Ameritech at 14; GTE at 7; Bell South at 8.

actually be enhanced if the Commission reduces the risk of strategic overinvestment by forebearing from exercising its Section 214 authority.

Section 214 review and price caps complement each other. The ability of price caps to sever the link between investment and prices would be diminished if the Commission were to forbear from applying its Section 214 procedures to price cap LECS. In order to meet the forbearance condition of not harming consumers, parties must make a stronger case for forbearance than "it would not result in rates increasing too much." Yet, that is the best one could hope for since forbearing from Section 214 procedures will increase incumbent LEC's incentive to overinvest because they would be partly compensated through the low-end sharing adjustment.

IV. Line Extensions Should be Narrowly Defined

In its Notice, the Commission tentatively defined a line extension as a line permitting a carrier to expand its service into geographic territory that it is eligible to serve, but where it does not currently reach. The Commission also defined a new line as an increase in the capabilities of a carrier's existing network.[8] MCI agreed with these definitions because they drew a clear line between cases where a dominant carrier can engage in anticompetitive investment practices to foreclose entry, and cases where a carrier is not able to do so.

The Commission noted that its distinction between line extension and new line may produce some anomalous results, but believed that use of its forbearance

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[8] *Notice* at para. 21.

authority will correct them.[9] Specifically, the Commission concluded that its definition would require an IXC that served the entire country to obtain Section 214 authorization before installing additional lines.[10] A number of parties have criticized this interpretation. For example, Ameritech argues that under the Commission's interpretation of its line extension definition, installing lines to a new sub-division within its service territory that is bordered by sub-divisions to which the carrier already provides service, would be considered new lines, rather than an extension of existing lines.[11] Ameritech argues that this interpretation defies common sense, and proposes a much broader definition of extension that essentially includes network augmentation.[12]

The Commission's interpretation of its definition is confusing, and may have caused it to precipitously choose to forbear from enforcing its Section 214 procedures. The Commission's confusion on this issue has created an opportunity for parties to propose anticompetitively broad definitions of line extension.[13] Contrary to the Commission's discussion, its definition of line extension does not require one to conclude that serving an unserved portion of a dominant carriers' service territory

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9 *Id* at para. 26.

10 *Ibid.*

11 *See*, Comments of: Ameritech at 8; GTE at 4;

12 *See*, Comments of: Ameritech at 8; GTE at 5; Pacific Telesis at 5.

13 For example, GTE proposes expanding the definition of line extension to include augmentation of a carrier's existing network: "An extension of a line within a carrier's network, adding to or expanding its existing network, could also be an extension of a line..." GTE Comments at 4.

would constitute a new line. Rather, the definition clearly states that installing lines within a carrier's service territory into heretofore unserved areas, is a line extension. An incumbent LEC that was authorized to serve an area, would be able to do so without Section 214 approval, so long as its investment resulted in the extension of its existing network into unserved territory, and so long as this extension did not involve an augmentation of its network. Of course, if the "extension" was accompanied by an augmentation of line or network to the heretofore unserved areas, then it would have to be considered a new line. Section 214 procedures would be necessary to ensure the carrier was not foreclosing entry by investing in excess capacity. The anomalous results parties refer to disappear when the Commission's distinction between line extension and new line are properly interpreted. There is no need to broaden the definition of line extension, or resort to forbearance to address the alleged anomaly.

V. Conclusion

For the above-mentioned reasons, MCI encourages the Commission to adopt the proposals suggested by MCI in its initial Comments and the interpretations offered in its Reply Comments.

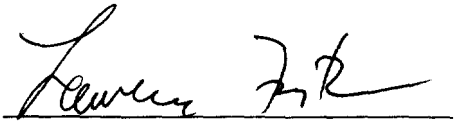
Respectfully submitted,
MCI TELECOMMUNICATIONS CORPORATION

Lawrence Fenster
MCI Telecommunications Corporation
1801 Pennsylvania Ave., NW
Washington, DC 20006
(202) 887-2180

March 17, 1997

STATEMENT OF VERIFICATION

I have read the foregoing and, to the best of my knowledge, information and belief, there is good ground to support it, and it is not interposed for delay. I verify under penalty of perjury that the foregoing is true and correct. Executed on March 17, 1997.



Lawrence Fenster
1801 Pennsylvania Ave., N.W.
Washington, D.C. 20006
(202) 887-2180

CERTIFICATE OF SERVICE

I, Johanna Schiappa, do hereby certify that a copy of the foregoing **Reply Comments** has been sent by United States first class mail, postage prepaid, hand delivery, to the following parties on this 17th day of March, 1997.

Reed E. Hundt**
Chairman
Federal Communications Commission
Room 814
1919 M Street, NW
Washington, DC 20554

Rachelle E. Chong**
Commissioner
Federal Communications Commission
Room 844
1919 M Street, NW
Washington, DC 20554

James H. Quello**
Commissioner
Federal Communications Commissioner
Room 802
1919 M Street, NW
Washington, DC 20554

Susan P. Ness**
Commissioner
Federal Communications Commission
Room 832
1919 M Street, NW
Washington, DC 20554

Regina Keeney**
Chief, Common Carrier Bureau
Federal Communications Commission
Room 500
1919 M Street, NW
Washington, DC 20554

Kathy Levitz**
Deputy Chief
Common Carrier Bureau
Federal Communications Commission
Room 500
1919 M Street, NW
Washington, DC 20554

Geraldine Matisse, Chief**
Network Services Division
Common Carrier Bureau
1919 M Street, NW
Washington, DC 20554

Marty Schwimmer**
Common Carrier Bureau
Network Services Division
1919 M Street, NW
Washington, DC 20554

Pat Degraba**
Chief Economist
Common Carrier Bureau
1919 M Street, NW
Washington, DC 20554

Diane Smith
ALLTEL Corporate Services, Inc.
655 15th Street, NW, Suite 220
Washington, D.C. 20005

Peter Jacoby
295 N. Maple Ave
Room 3250J1
Basking Ridge, NJ 07920

Mary McDermott
U.S. Telephone Association
1401 H Street, NW, Suite 600
Washington, DC 20005

Lucille Mates
Pacific Telesis Group
140 New Montgomery St
Room 1526
San Francisco, CA 94105

Gail L. Polivy
GTE Service Corporation
Suite 1200
1850 M Street, NW
Washington, DC 20036

Sam Cotten
Chairman
Alaska Public Utilities Commission
1016 W. Sixth Ave., Suite 300
Anchorage, AK 99501

Leon Kestenbaum
Sprint Corporation
1850 M St., NW, Suite 1110
Washington, DC 20036
Washington, DC

Robert M. Lynch
South Western Bell Telephone
Company
One Bell Center
Suite 3520
St. Louis, Missouri 6310

William Barfield
BellSouth Corporation
Suite 1700
1155 Peachtree Street, NE
Atlanta, GA 30309-3610

****Hand Delivery**

Michael Karson
Ameritech
Room 4H88
2000 West Ameritech Center Drive
Hoffman Estates, IL 60196

John Taylor
US West, Inc.
Suite 700
1020 19th Street, NW
Washington, DC 20036

Edward Shakin
Bell Atlantic
1320 N. Court House Rd.
8th Floor
Arlington, VA 22201

William Smith
NYNEX
1095 Ave of the Americas
Room 3725
New York, NY 10036

Raul Rodriguez
Leventhal, Senter & Lerman
2000 K St., NW, Suite 600
Washington, DC 20006

Alfred Mamlet
Attorney for TLD
Steptoe & Johnson
1330 Connecticut Ave., NW
Washington, DC 20036

International Transcription Service
2100 M Street, NW
Suite 140
Washington, DC 20037

Johanna Schiappa